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## ***Obama Administration FY 2015 budget focuses on tax reform, deficit reduction, and new initiatives***

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### ***In brief***

President Obama today submitted to Congress a \$3.9 trillion federal budget for Fiscal Year 2015. Like last year's budget, revenue proposals in the President's FY 2015 budget are separated into three categories – business tax reform, deficit reduction, and offsets for certain tax relief proposals and new programs.

The Administration does not provide a detailed tax reform plan but instead again proposes to reserve revenue from certain revenue raising proposals for "long-run revenue neutral business tax reform." The budget features several new revenue-raising proposals along with other previously-proposed international and domestic business revenue raisers that could offset part of the cost of business tax reform. The Administration continues to call for a top corporate rate of 28 percent, with \$150 billion in one-time revenue from tax reform to be used for infrastructure spending.

The budget proposes to make certain provisions permanent as part of tax reform, including a modified research credit, certain renewable energy tax provisions, and several temporary individual and small business tax provisions.

The President's budget calls for \$651 billion in increased revenues from upper-income individuals for deficit reduction. Additional deficit-reduction revenues are proposed to come from health savings, immigration reform, and lower interest payments on the debt. The Administration projects that under its budget the federal deficit will be reduced to 1.6 percent of GDP by FY 2024.

The budget calls for other revenue raising proposals to offset the cost of increased spending. The Administration proposes to offset the cost of an expanded Earned Income tax credit by changing the tax treatment of 'carried interest' and by changing self-employment tax rules. The budget also again proposes a cigarette tax increase to offset the cost of expanded preschool education programs.

The Treasury Department released a 297-page General Explanation of the Administration's FY 2015 Revenue Proposals (Green Book). Click [here](#) for a copy of the Treasury Green Book.

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## ***In detail***

### ***Tax reform***

While not providing a specific tax reform plan, the Administration's budget states that President Obama "believes that reforming our business tax code can help create jobs and spur investment, while ensuring a fairer and more equitable tax system that eliminates the loopholes that reward companies for moving profits overseas and allow them to avoid paying their fair share."

### ***New proposals:***

The President's budget includes several new revenue-raising proposals that would be reserved for tax reform. These new proposals would:

- Restrict deductions for excessive interest of members of a financial reporting group.
- Prevent avoidance of foreign base company sales income through manufacturing services arrangements.
- Create a new category of Subpart F income for transactions involving digital goods or services.
- Restrict the use of hybrid arrangements.
- Limit the application of exceptions under Subpart F for certain transactions that use reverse hybrids.
- Limit the ability of domestic entities to expatriate.
- Modify like-kind exchange rules for real property.
- Conform corporate ownership standards.
- Prevent elimination of earnings and profits through distributions of certain stock.

### ***Previously-proposed international tax measures reserved in the budget for tax reform include proposals that would:***

- Defer deductions of interest expense related to deferred income from foreign subsidiaries.
- Require pooling of foreign tax credits.
- Tax currently "excess returns" associated with transfers of intangibles offshore.
- Limit shifting of income through intangible property transfers.
- Modify tax rules for dual capacity taxpayers.
- Disallow deductions for excess non-taxed reinsurance premiums paid to foreign affiliates.
- Tax gain from the sale of a partnership interest on look-through basis.
- Prevent use of leverage distributions from related foreign corporations to avoid dividend treatment.
- Extend section 338(h)(16) to certain asset acquisitions.
- Remove foreign taxes from a section 902 corporation's foreign tax pool when earnings are eliminated.

### ***Other Administration revenue-raising proposals to be reserved for tax reform would:***

- Eliminate certain oil and gas preferences, including the domestic manufacturing deduction, expensing of intangible drilling costs, and percentage depletion.

- Eliminate certain coal preferences, including the domestic manufacturing deduction.
- Require that derivative contracts be marked to market with the resulting gain or loss treated as ordinary income.
- Modify treatment of insurance companies and products, including dividends-received deduction for life insurance company separate accounts.
- Repeal LIFO method of accounting
- Repeal lower-of-cost-or-market inventory accounting method.
- Modify depreciation rules for non-commercial general aircraft.
- Repeal gain limitation for dividends received in reorganization exchanges
- Expand the definition of built-in loss for purposes of partnership loss transfers.
- Extend partnership basis limitation rules to non-deductible expenditures.
- Limit the importation of losses under related-party loss limitation rules.
- Deny deduction for punitive damages

### ***Deficit reduction individual tax increases***

While not seeking any additional increases in individual tax rates, the President's budget proposes to reduce the federal deficit by:

- Limiting to 28 percent the value of all itemized tax deductions and certain tax exclusions, including tax-exempt interest, employer-sponsored health insurance, and retirement contributions, for

individuals with taxable incomes in the 33-percent, 35-percent, or 39.6-percent tax brackets. A similar limitation would apply under the alternative minimum tax. The Treasury Department estimates this proposal to raise \$598 billion over 10 years.

- Implementing a "Buffett Rule" 30-percent minimum tax, with carve-out for charitable giving. The proposed minimum tax would be phased in for modified adjusted gross income starting at \$1 million, and would be fully phased in at \$2 million. This proposal is estimated to raise \$53 billion over 10 years.

#### ***Other tax increase proposals***

The budget identifies several revenue-raising proposals to offset the cost of certain federal programs, including a new proposal to provide for reciprocal reporting of information in connection with the implementation of FATCA.

#### ***Additional proposed revenue offsets and 'loophole closers' include proposals to:***

- Tax 'carried interest' partnership income as ordinary income.
- Conform self-employment contributions act (SECA) taxes for professional services businesses, including S corporations, limited partnerships, general partnerships, and LLCs taxed as partnerships.
- Limit the total accrual of all individual retirement accounts (IRAs) and other tax-preferred retirement accounts; currently, the maximum permitted accumulation of tax-preferred retirement accounts for an individual age 62 would be approximately \$3.2 million.

- Reinstate the estate tax at 2009 levels, with a top rate of 45 percent and a \$3.5 million exemption.
- Establish a "financial crisis responsibility fee" on large financial institutions.
- Require current inclusion in income of accrued market discount and limit the accrual amount of distressed debt.
- Require that the cost basis of portfolio stock that is a covered security must be determined using the average basis method.
- Reinstate Superfund taxes.
- Make permanent the FUTA surtax.
- Increase certainty with respect to worker classification.
- Restrict deductions for certain conservation easements.
- Expand 'tax gap' compliance requirements.

#### ***Business tax proposals***

The budget includes several business tax proposals that are intended to provide incentives for manufacturing, research, clean energy, and infrastructure.

These business tax incentives include proposals to:

- Enhance and make permanent the research credit.
- Modify and permanently extend the renewable electricity production tax credit.
- Extend increased Section 179 expensing.
- Eliminate capital gains taxation on investment in small business stock.
- Modify and permanently extend the New Markets Tax Credit, and other regional growth incentives.

- Extend and modify the work opportunity tax credit.
- Provide tax incentives for locating jobs and business activity in the United States, and remove tax deductions for "shipping jobs overseas."
- Exempt certain foreign pension funds from FIRPTA rules.

The budget also includes several business tax simplification proposals, including:

- Repeal of Section 197 anti-churning rules.
- Repeal of the telephone excise tax.
- Repeal technical terminations of partnerships.
- Rationalization of tax return filing due dates so they are staggered.

#### ***Next steps***

Congress in December 2013 approved a two-year Bipartisan Budget Act setting spending levels for FY 2014 and FY 2015. Current law sets an April 15 deadline for the House and Senate to approve annual budget resolutions, but it is unclear whether the House and Senate will pass an FY 2015 budget resolution. For more on last year's budget agreement and the outlook for tax legislation in 2014, see the [WNTS 2014 Tax Legislative Outlook – Navigating a path forward](#).

While President Obama has renewed his call for business tax reform, House Ways and Means Committee Chairman Dave Camp (R-MI) on February 26, 2014 released a comprehensive tax reform discussion draft. For a detailed summary of Chairman Camp's discussion draft, see our February 28 [WNTS Insight – Overview of Ways and Means Chairman Camp's tax reform discussion draft](#).

Senate Finance Chairman Ron Wyden (D-OR) recently stated that he wants action in early 2014 to renew the research credit and other expired business and individual tax provisions as a “bridge” to tax reform.

### ***The takeaway***

Although Congress and President Obama continue to debate how to address federal deficits, all parties continue to call for significant tax

reform legislation. Businesses and individuals should review the tax reform proposals and continue to provide input to tax policymakers.

### ***Let's talk***

For a deeper discussion of how this might affect your business, please contact:

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